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PROTECTING OLDER AMERICANS AGAINST OVERPAYMENT OF INCOME TAXES

(Deductions You Are Entitled
To Use for 1989)

AN INFORMATION PAPER

PREPARED FOR USE BY THE

SPECIAL COMMITTEE ON AGING
UNITED STATES SENATE

JANUARY 1990

Serial No. 101-G

This document has been printed for information purposes. It does not offer findings or recommendations by this committee.

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PREFACE

To help assure that older Americans claim every legitimate income tax deduction, exemption, and tax credit, the Senate Special Committee on Aging, in cooperation with the Internal Revenue Service, has prepared this information paper for tax year 1989. On page 20 you will find pertinent information about the recent changes in the Medicare Catastrophic law. We hope this knowledge helps you in filling out your tax forms.

Keeping up with new tax provisions and filling out tax forms can be a very complicated process. In providing this information paper, the Senate Special Committee on Aging hopes to be of assistance to you.

DAVID PRYOR,
Chairman.
JOHN HEINZ,
Ranking Minority Member.

IRS ASSISTANCE IS AVAILABLE TO HELP YOU

Tele-Tax: The Internal Revenue Service has a telephone service called Tele-Tax. This service provides recorded tax information tapes on about 140 topics covering such areas as filing requirements, dependents, itemized deductions, and tax credits. Tele-Tax is available 24 hours a day, 7 days a week, to taxpayers who use push-button telephones. Rotary (dial) service is available Monday through Friday during regular office hours. A listing of tapes and instructions on how to use Tele-Tax are near the end of the tax form instructions.

Publications to assist you: The IRS prepares many free publications to help answer your tax questions. In addition to the general Publication 17, "Your Federal Income Tax," publications are available on specific topics, such as:

"Your Rights as a Taxpayer" (Publication 1).

"Tax Withholding and Estimated Tax" (Publication 505).

"Credit for the Elderly or the Disabled" (Publication 524).

"Highlights of 1989 Tax Changes" (Publication 553).

"Tax Information for Older Americans" (Publication 554).

"Tax Guide to U.S. Civil Service Retirement Benefits" (Publication 721).

"Tax Information for Handicapped and Disabled Individuals" (Publication 907).

"Guide to Free Tax Services" (Publication 910).

"Social Security Benefits and Equivalent Railroad Retirement Benefits" (Publication 915).

Single copies of the above publications can be ordered by mail, using the order form in your tax package or by calling IRS toll-free at 1-800-424-3676.

Other special IRS programs offering free assistance: Through the tax counseling for the elderly (TCE) program, IRS-trained volunteers assist individuals age 60 or older with their tax returns at neighborhood locations in many areas. In addition, certain volunteer income tax assistance (VITA) aides have been trained to help older Americans with their tax returns. (VITA assistance is also available to persons who cannot afford professional tax help as well as to military, handicapped, and non-English-speaking individuals.) The IRS toll-free number, 1-800-424-1040 can tell you where and when you can find TCE or VITA assistance in your area.

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WHO MUST FILE A FEDERAL TAX RETURN IS GENERALLY DETERMINED BY GROSS INCOME AND FILING STATUS*

You must file a return for 1989, even though you owe no tax if:	*And your gross income was at least:*
1. You were single and were:	
Under age 65	$5,100
Age 65 or older	$5,850
2. You were married filing a joint return and were living with your spouse at the end of 1989 or on the date your spouse died and:	
Both were under age 65	$9,200
One spouse was age 65 or older	$9,800
Both spouses were age 65 or older	$10,400
3. You were married filing a separate return or married but not living with your spouse at the end of 1989 or on the date your spouse died (regardless of age)	$2,000
4. You were unmarried or considered unmarried as of December 31, 1989, and you provided over half the cost of keeping up a home (the main home) for yourself and a dependent (See Head of Household on page 16 of Publication 17), and were:	
Under age 65	$6,550
Age 65 or older	$7,300
5. You were a qualifying widow or widower with a dependent child and:	
Under age 65	$7,200
Age 65 or older	$7,800

*Being blind does not change your filing requirement.

6. You received *any* advance earned income credit (EIC) payments from your employer(s) during 1989.
7. You were self-employed and your net earnings from this work were at least $400, then you must file a return to pay self-employment tax. This rule applies regardless of your age, whether or not you are receiving Social Security benefits, and even if you do not otherwise have to file a Federal tax return. You are self-employed if you carry on a trade or business as a sole proprietor, a member of a partnership, or an independent contractor. This includes certain part-time work that you do at home or in addition to your regular job.

   If you work for a church or a qualified church-controlled organization that elected exemption from Social Security taxes, you will have to pay self-employment tax if you are paid $100 or more in a year by the church or organization.
8. You can be claimed as a dependent on another taxpayer's return.

   As a dependent, you must file an income tax return if you are:

   (1) Single and—
   - Your earned income was more than $3,100 ($3,850 if 65 or older or blind); or
   - Your unearned income was more than $500 ($1,250 if 65 or older or blind; $2,000 if both 65 or older AND blind); or
   - Your gross income was more than the total of your earned income (up to $3,100) or $500, whichever is larger; plus $750 if 65 or older or blind ($1,500 if both 65 or older AND blind).

   (2) Married and—
   - Your gross income was at least $5 and your spouse files a separate return and itemizes deductions; or
   - Your earned income was more than $2,600 ($3,200 if 65 or older or blind); or

- You have unearned income and your gross income was more than $500 ($1,100 if 65 or older or blind; $1,700 if both 65 or older AND blind); or
- Your gross income was more than the total of your earned income (up to $2,600), or $500, whichever is larger: plus $600 if 65 or older or blind ($1,200 if both 65 or older AND blind).

9. You owe any tax on an IRA or a qualified retirement plan. See "Savings Incentives: Individual retirement arrangements," later.

You should file a return for 1989, even though you owe no tax if:

1. Income tax was withheld from your pay, so that you can get a refund of the tax withheld, even if you are not required to file a return.
2. You qualify for the earned income credit.

TAX FORMS

There are three forms for filing Federal tax returns—Form 1040EZ, Form 1040A, and Form 1040. A simplified tax return form, Form 1040EZ can be used only if:

Your filing status is single; you are not age 65 or older or blind; you claim no dependents; your taxable income is less than $50,000; your income is all from wages, salaries, tips, taxable scholarships and fellowships, and taxable interest of $400 or less; you do not have any adjustments to income; you do not itemize your deductions; you have no other taxes; and you do not claim any tax credits.

You should use this form if you meet these qualifications, because it is easier to fill out than the other forms. Most older Americans should use either Form 1040 or Form 1040A.

Form 1040A is used by single individuals, a qualifying widow(er) with dependent child, or married couples with taxable income of less than $50,000. This income must come from salaries, tips, taxable scholarships and fellowships, interest, dividends, and unemployment compensation. If you have taxable Social Security or equivalent Railroad Retirement benefits to report, you CANNOT use Form 1040A. The only adjustment to income that can be taken on the 1040A is the deduction for certain contributions to an IRA. Only the Credit for

Child or Dependent Care Expenses and the Earned Income Credit can be claimed on Form 1040A.

Form 1040 is used by all other individuals except nonresident aliens. Taxable Social Security, self-employment income, pensions, and annuities are some of the additional types of income for which you MUST use Form 1040. You also must use Form 1040 if you are claiming itemized deductions for home mortgage interest, medical expenses, State and/or local taxes, casualty losses, or employee business expenses. See "Checklist of Itemized Deductions for Schedule A (Form 1040)", later.

PRESIDENTIAL ELECTION CAMPAIGN FUND

You may voluntarily choose to have $1 of your taxes ($2 on a joint return) paid into this fund to help pay for Presidential election costs. Making this choice will not change the amount of tax you pay or the amount of refund you will receive.

SOCIAL SECURITY AND RAILROAD RETIREMENT TAXABILITY

Generally, you will owe taxes on some (but never more than half) of your Social Security and equivalent Railroad Retirement benefits if your total income minus half of your benefits exceeds $25,000 for single and married persons who live apart all year and do not file a joint return or $32,000 for married couples who file a joint return. Married couples who live together but file separate tax returns must include part of their benefits in taxable income regardless of the amount of their total income.

• *Social Security.*—You should receive Form SSA-1099, "Social Security Benefit Statement," if you received benefits in 1989. This form will show any deductions made by Social Security from your total benefits, such as Medicare premiums, repayments of prior-year overpayments, etc. If you do not receive an SSA-1099 by early February or you believe the statement to be incorrect, you should call the SSA toll-free number, 1-800-234-5772.

To estimate whether you must include any of your Social Security benefits in taxable income, add up your income from *all* sources including any tax-exempt inter-

est you may have received and one-half of your net benefits (Box 5 of your SSA–1099).

• If your total income is $25,000 or less and you are a single person or a married person filing separately and did not live with your spouse at any time during the year ($32,000 for married couples filing a joint return), then none of your benefits will be included.

• If your total income exceeds $25,000 and you are a single person or a married person filing separately and did not live with your spouse at any time during the year ($32,000 for married couples filing a joint return), then some of your benefits will be included. You will need to figure the taxable part of your benefits by using the worksheet on page 13 of the Form 1040 Instructions.

• If your total income exceeds $0 and you are a married person who lives together with your spouse during the year and files a separate tax return, then some of your benefits will be includible in taxable income. For more information, get Publication 915, "Social Security Benefits and Equivalent Railroad Retirement Benefits."

• *Railroad Retirement Benefits.* A Railroad Retirement benefit is comprised of up to four different parts. Before 1984, only the supplemental annuity was taxable. Beginning in 1984, the other three parts became taxable but each in a different way. Only the Social Security equivalent portion of tier I benefits is taxed in the same manner as Social Security benefits. Tier II and the non-Social Security equivalent portion of tier I benefits are fully taxable after they exceed your contributions which were deducted during your career. Vested dual benefits are also fully taxable.

The Railroad Retirement Board will send each beneficiary a Form RRB–1099 showing the equivalent tier I benefits paid. The Form RRB–W–2P covers the other three parts. If you receive both Social Security benefits and Railroad Retirement benefits, you should use the Railroad Retirement worksheet. More complete information can be found in Publication 575, "Pension and Annuity Income—Including the Simplified General Rule."

SALE OF YOUR MAIN HOME

If you sold your main home during the year, you must report the sale or exchange of your home on Form

2119, "Sale of Your Home." You may be able either to postpone paying tax on some or all of the gain or to exclude the gain from your taxable income. In either case, you must use Form 2119 to inform IRS that you meet certain qualifications. If you are unable to either postpone the tax on the gain or to exclude the gain from gross income, then the taxable gain for the sale is reported on Schedule D, "Capital Gains and Losses." You cannot deduct a loss on the sale of your home. The loss has no effect on the basis on your new home.

• *Postponement of Gain.*—If, within 2 years before or 2 years after the date of sale, you purchase (or build) and live in another main home that costs at least as much as the adjusted sale price of the old home, your entire gain on the sale is postponed at the time of the sale or exchange. You need not use the same funds received for the sale of your old home to buy or build your new home. The tax on the gain is postponed, not forgiven. Any gain not taxed in the year of sale is subtracted from the cost of your new home, giving you a lower basis in the new home.

• *Exclusion of Gain.*—Special rules apply to the sale of a main home by persons age 55 or older. If (1) you were age 55 or older on the date of the sale or exchange of your main home, (2) you owned and lived in the home for at least 3 years of the 5-year period ending on the date of the sale or exchange, and (3) you or your spouse (depending on your marital status on the date of the sale) have never excluded gain on the sale or exchange of a home after July 26, 1978; then, you may elect to exclude up to $125,000 ($62,500 if you are married filing separately) of the gain from gross income whether or not you purchase a new home.

In the case of a jointly owned home, both you and your spouse will meet the age, ownership, and use tests if:

- You hold the home either as joint tenants, tenants by the entirety, or as community property on the date of the sale or exchange;
- You file a joint return for the tax year in which you sell the home; and
- Either of you are 55 or older on the date of the sale and has owned and lived in the property as a main home for the required time before the sale or exchange.

If the home is not jointly owned, the spouse who owns the property must meet the age, ownership, and use tests. The other spouse must join in making the choice.

If you become physically or mentally unable to care for yourself and live in a nursing home or a State-licensed facility, you will be considered to have lived in your home as your main home during your stay in the facility if you have owned and lived in your home as your main home for a total of at least 1 year during the 5-year period. This exception applies to sales after September 30, 1988.

For more complete information, get Publication 523, "Tax Information on Selling Your Home."

SAVINGS INCENTIVES

Individual retirement arrangements.—An individual retirement arrangement (IRA) is a personal savings plan that lets you set aside money for your retirement. You may be able to deduct contributions you make to an IRA in whole, or in part, depending on your circumstances. Earnings on your IRA are not taxed until they are distributed to you. You may deduct the amount you actually contributed up to the lesser of your compensation that you must include in income, or $2,000 if either you (or your spouse) were not covered by an employer's pension plan. If you (or your spouse) were covered at any time during the year by an employer's retirement plan, your deduction may be further limited. Also, you may be able to make nondeductible contributions, which have a tax-free basis. You may also be eligible to make contributions to an IRA for your nonworking spouse. See Publication 590, "Individual Retirement Arrangements (IRA's)," for more information.

Keogh plans.—You must have net earnings from self-employment to claim a deduction for payments to a Keogh (H.R. 10) plan. For information on Keogh plans, see Publication 560, "Self-Employed Retirement Plans."

TAX WITHHOLDING AND ESTIMATED TAX PAYMENTS

The Federal income tax system operates on a pay-as-you-go basis. Typically, taxes are withheld from wages, salaries and other forms of compensation including some retirement payments. If taxes are not withheld

you are probably required to make quarterly payments to meet your estimated tax liability. Some examples of income from which income tax is not generally withheld are: interest and dividends; self-employment; alimony; rental income; capital gains; and the taxable portion of Social Security benefits.

• *Withholding on pensions and annuities.*—Unless you choose not to have any withheld, Federal income tax will generally be withheld from your taxable pension and annuity payments. This includes distributions from an individual retirement arrangement, from a life insurance company under an endowment, annuity, or life insurance contract, from a pension, annuity, or life insurance contract, from a pension, annuity, profit-sharing plan or from stock bonus plan, or from any similar plan that defers the time you receive compensation. The amount withheld depends on whether you receive payments spread out over more than 1 year (periodic payments) or whether you receive all of the payments within 1 year (nonperiodic payments).

Withholding from periodic payments of a pension or annuity is figured in the same way as withholding from salaries and wages. To tell the company that pays your pension or annuity how much you want withheld, fill out Form W–4P, or a similar form provided by the company, showing your marital status and the number of withholding allowances to which you are entitled. If you do not give the payer a Form W–4P, tax will be withheld as if you are married and claiming three withholding allowances. You may also use this form to tell the payer you do not want any tax withheld. However, if you are a U.S. citizen or resident alien whose residence address is in a foreign country, the payer must withhold tax.

Tax will be withheld at the rate of 10 percent on any nonperiodic payments you receive, unless they are part of a "qualified total distribution." A qualified total distribution is payment within 1 year of your entire interest in a pension, profit-sharing, stock bonus, or qualified annuity plan. The amount withheld from a qualified total distribution is specified in tables. The payer can tell you the amount that will be withheld.

Because the withholding rates for nonperiodic payments do not depend on withholding allowances or whether you are married or single, Form W–4P is not

used. The withholding rates are fixed; you cannot change the way tax is withheld. However, you can use Form W-4P to choose to not have tax withheld; to revoke a previous choice not to have tax withheld; or to specify that an additional amount be withheld.

• *Estimated tax requirements.*—Remember, if no tax or not enough tax is withheld from your income, you may need to pay estimated tax. Your estimated tax generally is the total of your expected income tax, self-employment tax, and other taxes reported on Form 1040, less your expected withholding and credits. Form 1040-ES provides a worksheet for making this computation.

If your estimated tax for 1990 is $500 or more and you expect your income tax withholding and credits to be less than the lesser of: (1) 90 percent of the tax liability shown on your 1990 return, or (2) 100 percent of the tax liability shown on your 1989 tax return (assuming the return covered all 12 months), you generally must pay an estimated tax and use Form 1040-ES. Installment payments are due April 16, June 15, September 15, and January 15, 1991. For more information, see Publication 505, "Tax Withholding and Estimated Tax."

TAX TABLE

You must use the Tax Table to find your tax if your taxable income (line 5, Form 1040EZ; line 19, Form 1040A; or line 37, Form 1040) is less than $50,000. You *must* use this table *unless* your taxable income is $50,000 or more. In that case, you must use the Tax Rate Schedules. The Tax Table is designed to be used by individuals whether or not they itemize their deductions.

EXEMPTIONS

You are allowed a $2,000 deduction for each exemption shown on your tax return (line 6e, Form 1040A or Form 1040). However, you may not take an additional exemption if you are age 65 or older or blind. Instead, you are allowed a higher standard deduction amount if you qualify. See the discussion on standard deduction.

If you can be claimed as a dependent on the tax return of another taxpayer, you are not allowed to claim your own exemption on your own tax return.

EXEMPTIONS FOR DEPENDENTS AND MULTIPLE SUPPORT AGREEMENTS

In general, a person may be claimed as a dependent of another taxpayer, provided ALL five tests are met: (1) Support, (2) gross income, (3) member of household or relationship, (4) citizenship, and (5) joint return. For more information, get Publication 50 "Exempting Standard Deductions, and Filing Information."

If all five dependency tests are met and you are entitled to claim a person as a dependent, that person may not claim his or her own exemption if he or she is required to file a tax return.

If you claim an exemption for a person who was age 2 or older on December 31, 1989, you must enter his or her Social Security number on your tax return. If your dependent does not have a Social Security number, you may obtain one by filing Form SS–5 with your local Social Security Administration office. If your dependent does not have a number by the time you are ready to file your return, apply for one and enter "Applied for" in the space for your dependent's Social Security number on your return.

• *Multiple Support Agreements.*—The support test is met if the person claiming the exemption contributed more than one-half of the individual's total support during the calendar year. But in some cases, two or more individuals provide support for an individual, and no one individual has contributed more than half the person's support. However, it still may be possible for one of the individuals to claim the $2,000 exemption if all of the following requirements for multiple support are met:

(1) Two or more persons—any one of whom could claim the person as a dependent if it were not for the support test—together contribute more than half of the dependent's support.

(2) Any one of those who individually contributes more than 10 percent of the mutual dependent's support, but only one of them may claim an exemption for the dependent.

(3) Each of the others who individually contributes more than 10 percent must sign a written statement that he or she will not claim the dependency exemption for that year. The statement must be filed with the

income tax return of the person who claims the dependency exemption. Form 2120, "Multiple Support Declaration," is used for this purpose.

Note. You can include with your medical expenses those medical expenses you paid for a person for whom you meet the support test under a multiple support agreement, even if you may not claim the person as a dependent because he or she had gross income of $2,000 or more.

STANDARD DEDUCTION

The standard deduction reduces your taxable income. It also reduces the need for many taxpayers to itemize their deductions. The standard deduction, which depends on your filing status and whether you are age 65 or older or blind, is not built into the Tax Table or Tax Rate Schedules but is figured separately. Once you have figured your standard deduction amount, you should then decide which gives you a higher tax benefit—taking the standard deduction or itemizing your deductions on Schedule A of Form 1040.

If you are age 65 or older or blind in 1989, you are entitled to a standard deduction amount which is more than the amount for taxpayers under 65 and not blind.

You are considered 65 for the 1989 tax year if your 65th birthday was on or before January 1, 1990. You are considered blind for 1989 if you are blind on the last day of 1989. Your tax instruction booklet has more information on the requirements.

Special rules. Your standard deduction is zero if your spouse itemizes deductions on a separate return, you are a dual-status or nonresident alien, or you have a short tax year. If you can be claimed as a dependent on another person's tax return, your standard deduction may be limited. If you meet one of these special rules, you may not use the standard deduction table which follows. See your tax instruction booklet for more details on these special rules. Unless you can be claimed as a dependent or meet one of the special rules, you may figure your standard deduction amount using the table that follows.

1989 Standard Deduction Table

Caution. This table does not apply to taxpayers who can be claimed as dependents.

STEP 1. Check the number of boxes that apply to you.

You	☐ 65 or older	☐ Blind
Your spouse	☐ 65 or older	☐ Blind

Total number of boxes you checked ..... ☐

STEP 2. Find your standard deduction.

If your filing status is:	and the number of boxes you checked in Step 1 above is:	your standard deduction is:
Single	0	$3,100
	1	3,850
	2	4,600
Married filing jointly	0	$5,200
	1	5,800
	2	6,400
	3	7,000
	4	7,600
Married filing separately [1]	0	$2,600
	1	3,200
	2	3,800
	3	4,400
	4	5,000
Head of household	0	$4,550
	1	5,300
	2	6,050
Qualifying widow(er)	0	$5,200
	1	5,800
	2	6,400

[1] If your spouse itemizes deductions on a separate return, your standard deduction is zero.

CHECKLIST OF ITEMIZED DEDUCTIONS FOR SCHEDULE A (FORM 1040)

MEDICAL AND DENTAL EXPENSES

Medical and dental expenses are payments you make for the diagnosis, treatment, or prevention of disease. They also include payments for treatment affecting any part or function of the body. Expenses for transportation to get medical care are included in medical expenses. Payments for insurance that provides medical care for you, your spouse, and dependents are included in medical expenses. Unreimbursed expenses are deductible to the extent they are more than 7.5 percent of your adjusted gross income (line 31, Form 1040). Expenses may be deducted only in the year you paid them. If you charge medical expenses on your credit card, deduct the expenses in the year the charge is made regardless of when the bill is paid.

Drugs and medicines.—Amounts paid for medicines and drugs that required a prescription, and for insulin are deductible. These items are included in medical expenses, subject to the 7.5-percent rule.

Expenses for the following are included in your medical and dental expenses:

—Doctors, surgeons, dentists, eye doctors, gynecologists, chiropractors, osteopaths, podiatrists, chiropodists, psychiatrists, psychologists, physical therapists, acupuncturists, Christian Science practitioners, and psychoanalysts.

—Medical examinations, X-rays and laboratory services, surgery, and dental fees.

—Nursing help. However, if you pay someone to do both nursing and housework, you may deduct only the cost of the nursing help.

—Hospital care (including meals and lodging), clinic costs, lab fees.

—Medical treatment (including meals and lodging) at a center for drug addicts or alcoholics.

—Medical aids such as hearing aids (and batteries), false teeth, eyeglasses, contact lenses, braces, artificial limbs, crutches, wheelchairs, guide dogs and the cost of maintaining these aids.

—Oxygen equipment and oxygen to relieve problems in breathing caused by a medical condition.

—Ambulance service and other travel costs to get medical care. If you used your own car, you may claim what you spent for gas and oil to go to and from the place you received medical care, or you may claim 9 cents a mile. Add parking fees and tolls to the amount you claim under either method.
—Cosmetic surgery.
—Cost and repair of special telephone equipment for the deaf.
—Extra cost of a specially equipped television set and the cost of an adapter for a regular set that provides subtitles for a deaf person.
—Part of the cost of braille books and magazines that is more than the price for regular books and magazines.
—Capital expenditures for medical purposes, such as air-conditioning or elevators. If these expenses are for permanent improvements that increase the value of the property, you may include them as medical expenses only to the extent that they cost more than the increase in the value of the property.
—Cost of a nursing home (including meals and lodging) if the principal reason for being in the nursing home is to get medical care.
—Medical care included in the "life-care fee" or "founders fee" of a retirement home that is paid monthly or as a lump sum under an agreement with the home. The deductible part of the fee payment is the amount set apart for medical care.
—Cost of special equipment, such as a motorized wheelchair or autoette, special hand controls and other special equipment installed in a car specifically for the use of a physically handicapped person.

You may only deduct those medical expenses that are more than 7.5 percent of your adjusted gross income.

For more information, see Publication 502, "Medical and Dental Expenses."

TAXES

- Real estate
- Personal property
- State, local, or foreign income

INTEREST

- Personal loan
- Home mortgage
- Auto loan
- Loans on life insurance
- Installment purchases

For 1989, you may deduct only 20 percent of the interest you paid on loans used for personal purposes, other than qualified home mortgage interest. In most cases, you will be able to deduct all of your home mortgage interest. Whether your home mortgage interest is fully deductible depends on the date you took out the mortgage, the amount of the mortgage, and your use of its proceeds. For more information, see Publication 936, "Limits on Home Mortgage Interest Deduction."

Bank and other general purpose credit cards.—If the credit is used for personal purposes, you may deduct 20 percent of the finance charge added to your monthly statement if no part of the charge was for investigation fees, membership fees, loan fees, service charges, or similar charges.

Points.—When buying a home, "points" may be interest paid in advance or charges for specific services. If the points are charges for specific services they are not deductible. You may deduct the amount you pay as points (provided they are prepaid interest), in the year of payment if the loan is used to buy or improve your main home and is secured by that home. In addition, the payment of points must be an established business practice in the area where the loan was made, the points must not exceed the number of points generally charged in your area, and the points are paid with funds other than those obtained from your lender.

If the home you purchase is not your main home, you may not deduct the full amount of points in the year paid. Instead, the prepaid interest paid as points must be spread over the life of the mortgage, and is deductible over that period.

Points are not deductible if they represent charges for services rendered by the lending institution (e.g., VA or FHA points are not deductible as interest if paid for specific services). Also, points are not deductible if paid by the seller but are selling expenses that reduce the amount realized.

Penalty for prepayment of a mortgage.—This is generally deductible as home mortgage interest if it qualifies. Otherwise, you may deduct it as personal interest.

Revolving charge accounts.—If the account is used for personal purposes, 20 percent of the finance charges

may be deducted if they are separately stated on your bill.

CONTRIBUTIONS

In general, contributions to qualified organizations, such as those organized and operated for religious, charitable, educational, scientific, or literary purposes may be deducted up to 50 percent of your adjusted gross income (line 31, Form 1040). Contributions "for the use of" any charitable organization or contributions to veterans organizations, fraternal societies, or nonprofit cemetery companies are limited to 30 percent of adjusted gross income (line 31, Form 1040).

If your total contributions for the year are 20 percent or less of your adjusted gross income (line 31, Form 1040), they are fully deductible (provided they otherwise qualify) and it is not necessary to figure whether the limits apply.

To deduct your contributions, you must make them in cash or other property before the close of your tax year. Other property (clothing, books, furniture, etc.) is deducted at the fair market value. You may deduct contributions you charge to your credit card in the year the charge is made.

Examples of other charitable contributions include:

—The cost and upkeep of uniforms that you must wear while performing donated services for a charitable organization.

—Out-of-pocket expenses you pay in giving services to a charitable organization. (Do not deduct the value of your time or services.)

—Payment of more than fair market value to an organization for goods, merchandise, services, banquets, shows, sporting events, etc.

—You may also deduct unreimbursed out-of-pocket expenses directly related to services you give to a charitable organization, such as gas and oil for your car. If you do not want to deduct actual expenses, you may use a standard rate of 12 cents a mile. In either case you may deduct parking fees and tolls.

Charitable contributions may only be claimed as an itemized deduction on Schedule A (Form 1040). You must keep records to prove your cash and noncash contributions. If your total noncash contributions are over $500, you must attach Form 8283, "Noncash Charitable

Contributions," to your return. For more information, see Publication 526, "Charitable Contributions."

CASUALTY OR THEFT LOSSES

You may deduct casualty losses, such as those that result from a tornado, flood, storm, fire, or auto accident (provided it was not caused by a willful act or willful negligence), or theft losses. The amount of your casualty loss deduction is generally the lesser of (1) the decrease in fair market value of the property as a result of the casualty or theft, or (2) your adjusted basis in the property before the casualty or theft. This amount must be reduced by any insurance or other reimbursement you receive.

Your nonbusiness casualty or theft losses are deductible only to the extent that your total losses during the year exceed 10 percent of your adjusted gross income after reducing each separate casualty or theft by $100. You must use Form 4684 to figure your casualty or theft loss. Report your casualty or theft loss on Schedule A (Form 1040).

You may not deduct a casualty or theft loss that is covered by insurance unless you filed a timely insurance claim for reimbursement. However, even if you did not file an insurance claim, you may deduct the part of the loss not covered by insurance. For more information, see Publication 547, "Nonbusiness Disasters, Casualties, and Thefts."

MISCELLANEOUS DEDUCTIONS

Unreimbursed employee expenses, expenses of producing income, and other qualifying expenses are deducted as miscellaneous itemized deductions on Schedule A (Form 1040). Most miscellaneous itemized deductions are subject to a 2 percent limit. The amount deductible is limited to the total of these miscellaneous deductions that is more than 2 percent of adjusted gross income. The 2 percent limit is applied after all other deduction limits are considered. Some of the expenses subject to the 2 percent limit are as follows:

—Professional society dues.
—Employment-related educational expenses.
—Expenses of looking for a new job.
—Professional books, magazines, journals, and periodicals.

—Work clothes and uniforms.
—Union dues and fees.
—80 percent of unreimbursed business-related meal and entertainment expenses.
—Certain other unreimbursed employee business expenses.
—Safe deposit rental.
—Tax preparation fees.
—Certain investment expenses.

Certain miscellaneous expenses are not subject to the 2 percent limit. These expenses include:

—Federal estate tax on income in respect of a decedent.
—Certain deductions when a taxpayer repays amounts held under a claim of right.
—Amortizable bond premiums on bonds acquired before October 23, 1986.
—Gambling losses to the extent of gambling winnings.
—Unrecovered investment in a pension when the retiree dies before the entire investment is returned.
—Impairment-related work expenses of a handicapped individual that are for deductible attendant care services at the individual's place of work and other expenses in connection with the place of work that are necessary for the individual to be able to work.

For more information, see Publication 529, "Miscellaneous Deductions."

TAX CREDITS

Tax credits are used to reduce the amount of tax you owe. All credits must be taken on Form 1040, with the exception of the Credit for Child and Dependent Care Expenses and the Earned Income Credit which may be taken on Form 1040A. No credits may be taken on Form 1040EZ.

The most common credits are:

CREDIT FOR CHILD AND DEPENDENT CARE EXPENSES

A portion of certain payments made for child and dependent care may be claimed as a credit against tax.

If you maintained a household that included your dependent under age 13 *or your disabled dependent, or your disabled spouse,* you may be allowed a tax credit

for employment-related child and dependent care expenses. These expenses must have been paid during the tax year in order to enable you to work (and your spouse if you were married) or to look for work. You must have income from work during the year. The maximum amount of child and dependent care expenses that may be used to compute the credit is $2,400 for one qualifying person and $4,800 for two or more qualifying persons.

The credit is 30 percent of your qualifying expenses if your adjusted gross income (line 31 of Form 1040 or line 13 of Form 1040A) is $10,000 or less. The 30-percent rate is reduced by 1 percent for each additional $2,000 (or part of $2,000) of adjusted gross income above $10,000 until the percentage is reduced to 20 percent for adjusted gross income above $28,000.

See the Form 1040A instructions or, if you file Form 1040, see Form 2441 for more information, including a special rule for divorced or separated taxpayers.

Also, you must include the name, address, and taxpayer identification number (unless it is an exempt organization) of the care provider on your tax return.

CREDIT FOR THE ELDERLY OR THE DISABLED

You may be able to claim this credit if you are: (1) Age 65 or over, or (2) under age 65 and retired on a permanent and total disability for which you receive taxable disability benefits in 1989, and under the mandatory retirement age.

For more information, see the instructions for Schedule R (Form 1040).

EARNED INCOME CREDIT

If you have a child who lives in your main home in the United States for more than half the year with you (for the entire year if the child is a foster child or if your filing status is qualifying widow or widower with dependent child), you may be entitled to a special payment or credit of up to $910. This is called the earned income credit. It may come as a refund check or be applied against any taxes you owe. Generally, if your earned income and your adjusted gross income were each less than $19,340 in 1989, you may be able to claim the credit.

Earned income means wages, salaries, tips, strike benefits, other employee compensation, certain disability pensions, nontaxable military quarters and subsistence allowances, and net earnings from self-employment. Your filing status must be married filing jointly, or qualifying widow(er) or head of household. However, certain married persons living apart with a dependent child who qualify for head-of-household status may also be eligible to claim the credit. For more information, see Publication 596, "Earned Income Credit."

MEDICARE CATASTROPHIC COVERAGE SUPPLEMENTAL PREMIUM

Congress has repealed the Medicare Catastrophic Coverage Supplemental Premium (the "Surtax"). You do not have to pay it in either 1989 or 1990. But, the tax forms and instructions were printed before the premium was repealed. If you use Form 1040, skip line 54. If you use Form 1040A, skip line 23.

If you increased estimated tax payments or tax withheld to pay the premium for 1989, include these amounts on the appropriate lines. If you overpaid your tax for 1989, you can claim a refund when you file your 1989 tax return. You may want to adjust your 1990 estimated tax payments since the premium has been repealed.

1990 INCOME TAX ITEMS OF INTEREST TO OLDER AMERICANS

Recent legislation made many changes to the tax law which affect the 1990 tax year. Some of the tax changes are as follows:

1. *Exemptions.*—The personal exemption increases to $2,050 for 1990.

2. *Standard deduction.*—For 1990, the standard deduction is $3,250 for single taxpayers; $2,725 for married filing separate taxpayers; $4,750 for head of household taxpayers; and $5,450 for qualifying widows and widowers, and married taxpayers.

If you are age 65 or older or blind in 1990, you are allowed an additional standard deduction amount depending on your filing status.

3. *Personal interest.*—For tax year 1990, only 10 percent of personal interest (such as interest on car

loans or credit card balances) can be deducted as an itemized deduction.

4. *Earned income credit.*—For 1990, the maximum earned income credit is increased to $953.40. The income limitation is increased to $20,264.

5. *Filing requirements.*—The amount of gross income you may receive before you are required to file a tax return has increased and is shown below. The chart below does not apply if you can be claimed as a dependent or you are self-employed.

Filing status	*Gross income*
Single:	
Under age 65	$5,300
Age 65 or older	$6,100
Married Filing Joint Return:	
Both spouses under age 65	$9,550
One spouse age 65 or older	$10,200
Both spouses age 65 or older	$10,850
Not living with spouse at the end of year (or on date spouse died)	$2,050
Married Filing Separate Return	$2,050
Head of Household:	
Under age 65	$6,800
Age 65 or older	$7,600
Qualifying Widow(er):	
Under age 65	$7,500
Age 65 or older	$8,150

6. *Interest exclusion for qualified U.S. savings bonds.*—Beginning in 1990, all or part of the interest from certain U.S. savings bonds can be excluded from income if you pay qualified higher education expenses during the year you redeem the bonds. The bonds must have been issued after 1989 to an individual age 24 or older. Qualified higher education expenses are tuition and required fees at a college or eligible vocational school for the bonds' owner or the owner's spouse or dependent. For more information, see Publication 550, "Investment Income and Expenses."

For more information on changes for tax year 1990, see Publication 553, "Highlights of 1989 Tax Changes."

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